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SUBJECT: U.S.-Involved Tender Dispute: Winning Twice Is Not Enough

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1. (SBU) SUMMARY AND COMMENT: L-Systech, a Mongolian-South Korean JVC, supported by an American consultant and vending U.S.-produced solar power equipment, saw its winning of an US\$8 million Government of Mongolia solar-power equipment tender frustrated by the improper and perhaps illegal behavior of the Mongolian Minister of Fuel and Energy B. Erdenebat. Concerted efforts by the JVC, post, and sympathetic individuals in the Ministry of Finance helped the JVC win a smaller tender for US\$6.5 million, but the Ministry of Fuel and Energy continues to stall on the contract and the issuance of funds. Post recommends that the upcoming TIFA talks be used to push the Mongolian government to resolve this dispute and to review the wider question of weakness in the Mongolian procurement system. Septel notes that ongoing efforts to resolve this specific dispute have uncovered problems with the GOM procurement system that may threaten its financial stability and ability to deliver quality projects on time and on budget. End Summary.

A Bright and Shiny Tender  
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2. (SBU) Just before the 2006 Thanksgiving Holiday, Ms. Grace Roberts, one of Mongolia's Honorary Consuls in California, met with CommOff regarding a troubled a solar power tender announced and administered by the Mongolian Ministry of Fuel and Energy (MFE). She and a consortium of three South Korean firms and their Mongolian partners, L-Systech, had participated in and in early November ostensibly won the US\$8 million contract to provision some 50,000 rural herder families in Mongolia solar power equipment. The government of Mongolia (GOM) was to pay for half of the cost and the herders were to cover the remaining 50%, making the total value of the program some US\$16 million. According to Ms. Roberts, U.S.-based solar power equipment manufacture Morningstar would sell the equipment to L-Systech, and Ms. Roberts would receive a consultant's fee for successfully assisting with the tender.

3. (SBU) So far so good, but upon the MFE Evaluation Committee's (EC) announcement of contract award to L-Systech, MFE Minister B. Erdenebat immediately annulled the result and urged the EC to award the contract to a South Korean firm although its bid was substantially more costly to the GOM than L-Systech's. Roberts

claimed that the Minister Erdenebat had some sort of improper financial arrangement with the losing firm, but could not document a precise relationship. Ms. Roberts and her Mongolian colleagues attempted to resolve dispute on their own and, failing in that effort, decided to ask for post's advice and support to move MFE to reconsider its annulment. (Note: Minister Erdenebat is the head of the Motherland Party, a small-time player offered three ministerial seats in return for supporting the current Enkhbold government. The party is often termed the "Erel Party," because of its close affiliation with the Erel company, a gold mining, banking and insurance firm headed by Erednebat. Like recently-dismissed ministers Jargalsaikhan and Gundalai, Erdenebat's tenure at his ministry has been embroiled in charges of corruption and conflict of interest, regarding proposed power plants and coal deposits, hydro-electric projects being built by his firms, and environmental degradation at his company's placer gold mines.)

#### Ministerial Mischief Surprises No One

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14. (SBU) Commoff brought Ms. Robert's concerns to contacts at MFE and the Ministry of Finance (MinFin). The MFE contact, a long-serving staffer, did not disagree with claims that the current minister might have acted improperly in this specific case. The official opined that some problems were beyond his capacity to solve. At MinFin, Ms. Kh. Mart (Director General of the Procurement Policy and Coordination Department) was less circumspect, stating, without elaborating, that she found Ms. Roberts's claims of Erdenebat's improprieties completely credible. In the meantime, Minister Erdenebat himself had gone public with his decision, announcing in print and on TV that he had to cancel the results because L-Systech was too small, that the firm's technology was ill-suited to the task at hand, and that the firm was too recently founded to be allowed to compete. Of course, Roberts and company

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rejected each of these points, noting that the EC had not only approved their technical qualifications but had awarded them the contract.

15. (SBU) Commoff then advised L-Systech to resolve the dispute through MinFin's newly established Dispute Resolution System, in which a panel of three professional evaluators selected by MinFin and each of the disputants would attempt to arbitrate the dispute. The results of the arbitration are not binding, as any of the parties (except MinFin) may opt for judicial review at any time. Mart welcomed our use of the new arbitration system and offered frank assessments of the solar procurement issue. She disputed each of Minister Erdenebat's claims that L-Systech was unsuitable, noting that her division agreed with the EC's initial judgment that L-Systech had satisfied all technical and financial requirements and that Minister Erdenebat had no basis for his annulment. She stated and showed us the official order in which Minister of Finance Bayartsaikhan had directed MFE to honor the initial award, which Minister Erdenebat had bluntly refused to do in direct contravention of the procurement rules and law of Mongolia.

16. (SBU) On post's advice, Roberts contacted the Mongolian Embassy in Washington, D.C., the Minister of Finance, the Prime Minister's office, and the Ministry of Industry and Trade. Ms. Roberts told Commoffs that the Mongolian Embassy had criticized her actions, urging her avoid publicizing her troubles and not to tell the U.S. Embassy anything about the event. The other GOM ministries murmured sympathetically about MFE's irregularities, but the Enkhbold government did nothing, as it has done in the face of most ministerial misbehavior.

#### Try, Try Again

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17. (SBU) In late November, Minister Bayartsaikhan announced that the GOM would uphold the annulment on budgetary grounds. MFE had stated that the budget available for the solar project was insufficient to fund US\$8 million in equipment, and MFE would re-tender the project for US\$6.5 million. Bayartsaikhan then officially informed L-Systech that he concurred with MFE's assessment of its budgetary

woes and was forced to annul the results of the first tender and support a second tender in line with available funds. He concluded his letter by inviting L-Systech to join in the second tender.

¶18. (SBU) Commoft met with Mart on December 1, concerning the GOM's decision. Mart confirmed that MFE had in fact seriously miscalculated its budget and was within its rights to re-tender the contract in line with actual funds on hand. However, she was extremely critical of Erdenebat and his staff for not monitoring their budget properly in the first place, stating without providing examples that MFE had done this a great deal over the last year, as had other unnamed ministries and agencies. She further added that this sort of ministerial "incompetence" and rule breaking had led to over thirty law suits in over as many tenders in 2006 alone, involving tens of millions of dollars in disputed contracts.

¶19. (SBU) On December 11, L-Systech reluctantly agreed decided to compete in Tender #2 and won again on December 13. Again, Minister Erdenebat attempted to annul the results and transfer the contract to the same higher-cost South Korean firm. He again cited L-Systech's recent formation and "inappropriate" technology as reasons for his decision. This time, however, MinFin bluntly ordered MFE to honor the results of Tender #2, noting that the EC had yet again ruled in favor of L-Systech on all counts and that the Minister had absolutely no legal basis to cancel the results. According to sources in MFE and Mart, several EC members had remonstrated with Erdenebat, noting that he had his bite at the apple, had failed, and should let this one pass because the Americans and their Embassy were complaining too much.

¶10. (SBU) Since mid-December, problems have continued to plague the contract, which presently is at an impasse. First, two losing companies sued MFE, emphasizing Mart's claim that MFE's poor process gives rise to law suits and frustrating, costly delays. MFE asserts that it had to revise the contract, but has refused to give L-Systech the revised contract. MFE demanded instead that the firm supply the solar systems without a corrected, binding contract.

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L-Systech won't manufacture and vend any system without a valid contract in hand.

¶10. (SBU) With half a loaf, L-Systech grumpily accepts that we have collectively salvaged something out of the debacle. Post will continue to press the GOM to honor its obligations in this matter, using the upcoming March TIFA talks to emphasize our concerns. We also recommend that this dispute be used by USG TIFA participants to make a wider, frank critique about how general weaknesses in the GOM's procurement system are negatively affecting Mongolia's reputation and business climate. Finally, Ms. Mart expressed embarrassment and disappointment that a procurement system that she had worked so hard to improve and had taken pride in had failed. She offered to take Commoft through the evolution of procurement law in Mongolia with an eye to alerting post to problems on the horizon for GOM procurement. Results of these discussions are detailed in septel.

Goldbeck